

**Brazil Focus –**  
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**Weekly Report**  
Aug. 26-Sept. 1  
2017

**Looking Ahead ➔ What to watch for?**

- **4ª Sept.** -- IBGE to announce July industrial production ➔ +0.0% MoM & - % YoY
- **4ª Sept.** -- Labor Day (National Holiday in US)
- **5-6 Sept.** -- Copom Meeting, Selic rate ➔
- **6-7 Sept.** -- XXI CAF Conference, Mayflower Hotel, Washington, DC
- **7ª Sept.** -- Independence Day [National Holiday, Brazil]
- **8ª Sept.** -- FGV to post August IGP-DI ➔ +0.0%,
- **8ª Sept.** -- IBGE to post August IPCA ➔ +0.0%; 12-month accumulation at %
- **8ª Sept.** -- IBGE ➔ industrial production data for July ➔ +0.0% MoM
- **13ª Sept.** -- IBGE - Retail Sales in July -0.0% MoM and - % YoY
- **13ª Sept.** -- Lula to testify before Judge Sérgio Moro in Curitiba
- **13ª Sept.** – TRF-4 will deliberate appeal by José Dirceu
• 15\textsuperscript{th} Sept. -- IBGE – Services Sector for July ➔ +0.\% MoM but - % YoY
• 16-19 Sept. -- International Trade Administration, ASIS 2017, Dallas, TX
• 18\textsuperscript{th} Sept. -- PGR – Raquel Dodge will replace Rodrigo Janot
• 19\textsuperscript{th} Sept. -- State Holiday in Rio Grande do Sul [Farroupilha Day]
• 19\textsuperscript{th} Sept. -- Central Bank ➔ July IBC-Br -0.\% & - % in 2016
• 22\textsuperscript{nd} Sept. -- IBGE to post IPCA-15 ➔ +0.\% vs +0.\% in August
• 22\textsuperscript{nd} Sept. -- Caged data for August ➔ jobs lost versus July
• 23\textsuperscript{rd} Sept. -- Pres. Michel Temer to celebrate his 76\textsuperscript{th} birthday

1 - POLITICS

1.1 – Amazonino elected Governador of AM

As expected (by the election polls), Amazonino Mendes (PDT), age 77, was elected governor of Amazonas in the second round runoff election on Sunday, 27\textsuperscript{st} August with 59.59\% of the valid vote. Senator Eduardo Braga (PMDB) polled 40.41\%. Mendes will serve out the remaining 14 months of the term of governor. This is the fourth time that Amazonino is elected governor.

<table>
<thead>
<tr>
<th>Candidates</th>
<th>First Round Total</th>
<th>%</th>
<th>Second Round Total</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amazonino (PDT)</td>
<td>577,397</td>
<td>38.77%</td>
<td>782,933</td>
<td>59.21%</td>
</tr>
<tr>
<td>E. Braga (PMDB)</td>
<td>377,680</td>
<td>25.36%</td>
<td>539,318</td>
<td>40.79%</td>
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<tr>
<td>Others (6)</td>
<td>534,281</td>
<td>35.87%</td>
<td>- -</td>
<td>- -</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,489,358</strong></td>
<td><strong>100.00%</strong></td>
<td><strong>1,322,251</strong></td>
<td><strong>100.00%</strong></td>
</tr>
<tr>
<td>Blank</td>
<td>61,826</td>
<td>- -</td>
<td>70,441</td>
<td>- -</td>
</tr>
<tr>
<td>Null</td>
<td>218,000</td>
<td>9.32%</td>
<td>342,280</td>
<td>14.63%</td>
</tr>
<tr>
<td>Abstention</td>
<td>569,501</td>
<td>24.35%</td>
<td>603,914</td>
<td>25.82%</td>
</tr>
<tr>
<td><strong>Electorate</strong></td>
<td><strong>2,338,886</strong></td>
<td><strong>100.00%</strong></td>
<td><strong>2,338,886</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

Apparently, in this supplementary election, the electorate was quite “alienated” where the 25\% abstention surpasses the vote total of the second place candidate in the second round that had 160,000 fewer valid votes than in the first round. In the second round Abstention+Nulls+Blanks accounted for 43.46\% of the electorate, where 56.53\% of the electorate cast valid votes.

In the general election in 2014, in the second round for Governor the TRE-AM totaled 503,405 abstentions, 26,208 Blanks, and 129,621 Nulls.

1.2 – Lava Jato
This time it was the PMDB’s turn and four of its senators were accused by the PGR this week.

1.2.1 – José Serra

On Monday, 28th August, STF Judge Rosa Weber accepted the accusation against Sen. José Serra (PSDB-SP) regarding the campaign finance for his presidential candidacy in 2010 and authorized an investigation by the Federal Police. In his plea bargaining testimony, Joesley Batista (JBS) affirmed that he made a R$ 20 million contribution to Serra’s campaign but only R$ 13 million was formally declared and the rest (R$ 7 million) became *Caixa Dois.*

1.2.2 – Romero Jucá

For the third time in 7 days, on 28th August the PGR accused Sen. Romero Jucá (PMDB-RR) of corrupt practices – accepting a R$ 150,000,00 bribe from Odebrecht for his “assistance” in the deliberation of MPs that interested Odebrecht.

1.2.3 – Renan Calheiros

On 28th August, STF Judge Luiz Roberto Barroso accepted the PGR’s accusation against Sen. Renan Calheiros (PMDB-AL) regarding his involvement in the “rip off” of Postalis – the pension fund of Brazil’s post office. See Item 1.5

1.2.4 - Henrique Alves

On 29th August, the plea bargaining of Fred Queiroz became public. He was one of the main campaign operators for Henrique Alves run for governor of Rio Grande do Norte in 2014. Queiroz affirmed that some R$ 7 million was used in the campaign to “buy” the support of local mayors and politicians and that these funds were donated by Joesley Batista (JBS). Alves served as a cabinet minister with Dilma Rousseff and also Michel Temer – until these accusations caused him to resign in 2016.

1.2.5 – Lúcio Funaro

On 29th August, STF Judge Edson Fachin received the full plea bargaining testimony by Lúcio Funaro who was the main operator and money changer for the PMDB. Reportedly, this testimony contains some devastating information about the involvement of Michel Temer in the PMDB operations”. Apparently, the PRG Rodrigo Janot is awaiting access to this testimony in order to prepare his second accusation (denunciation) against Temer to be filed at the STF – reportedly on 6th September. However, late Wednesday afternoon, STF Judge Edson Fachin returned the Funaro testimony to the PGR to do some “readjustments”. On 31st August, the PGR returned this “adjusted” file to the STF.

⇒ Stay tuned!!!
1.2.6 – Pasadena Refinery

On 30th August, the TCU convicted former Petrobras President José Sérgio Gabrielli and former Petrobras Director for International Affairs Nestor Cerverá and ordered them to return US$ 79 million regarding the losses incurred when Petrobras purchased the decrepit petroleum refinery in Pasadena, Texas – considered the ”worst business deal in the world”. Also, the TCU applied a R$ 10 million fine on both. However, at that time Dilma Rousseff was President of the Petrobras Administrative Council, but the TCU declared her exempt (not guilty) of involvement in this corruption scheme.

1.2.7 – Rodrigo Tacla Duran versus Sérgio Moro

Lawyer Rodrigo Tacla Duran worked for Odebrecht (2011-2016) as an “operator” of “secret” bank accounts in Europe used to pay bribes. He was accused by Brazilian Federal Prosecutors and an arrest warrant was issued by Judge Sérgio Moro. He was arrested in Spain in November 2016 but was released in January 2017 (he has dual Spanish citizenship). Duran tried to do plea bargaining, but this was not accepted by Brazilian prosecutors. Now, Duran is concentrating on producing accusations against the Lava Jato task force.

On 27th August, Duran released some harsh accusations. He alleged that labor lawyer Carlos Zucolotto Junior, a close friend of Judge Sérgio Moro (also a godfather/witness at Moro’s wedding) had operated parallel intermediations (negotiations) for Duran with the Lava Jato task force. Moro’s wife, Rosangela, had been a partner in Zucolotto’s law office and he defends Lava Jato prosecutor Carlos Fernando dos Santos Lima in a case being deliberated at the STJ.

Duran alleged that Zucolotto articulated a “reduction” of Duran’s sentence and his fine in return for his plea bargaining testimony. In return, Zucolotto would be paid via a “Caixa Dois” scheme that would be used to compensate persons who “assisted” in this negotiation. Duran claims that he has correspondence with Zucolotto that prove these articulations and will publish all this in a book.

Prosecutor Carlos Fernando dos Santos Lima explained that his lawyer for the STJ case is Vicente Paula Santos and Zucolotto is a partner in the same law firm as Paula Santos.


Want more? In an apparent “close articulation”, well known, flamboyant [and very expensive] criminal lawyer in Brasília who has defended many “notorious” persons accused of corruption (including in Lava Jato) – Antonio Carlos de Almeida Castro [Kakay] – on the same day (27th August) declared that Judge Sérgio Moro “should be placed under preventative arrest” because of the accusations of Tacla Duran. After a number of fierce court-attacks, Kakay backed off and declared that he “was misquoted”.
1.3 – Federal Police operations

This week the Federal Police carried out two anti-corruption operations

1.3.1 – Operation Alcmeon

On Wednesday morning, 30th August, the Federal Police carried out Operation Alcmeon in Recife, Natal and Mossoró with 23 warrants – two arrest warrants, 8 coercive testimony and 13 search-and-seize warrants. The focus is on the decision making process at the TRF-5, regional federal court in Recife. Allegedly, a corruption scheme operated to “buy” decisions regarding arrests, prison terms and confiscated assets. This scheme was revealed via plea bargaining testimony by a businessman who had “purchased” advantages. Apparently, persons accused/convicted by Lava Jato are involved. This is a very serious case of alleged corruption within a Regional Federal Court.

One of those arrested was retired TRF-5 Judge Francisco Barros Dias, accused of receiving a R$ 150,000,00 bribe.

1.3.2 – Operation Cancela Livre

In cooperation with the TCU, on 30th August, the Federal Police carried out Operation Cancela Livre --Open [Free] Toll Station with warrants in Rio Grande do Sul, Paraná and São Paulo. This operation investigates the case of some R$ 100 million over-invoicing in the construction of fourth lane of the Freeway (BR-290) between Proto Alegre and Gravataí (RS).

Cancela Livre refers to a norm imposed by the ANTT on highway concession holders that if the lines of cars at toll gates exceed 10 minutes, the toll gates must be opened to allow the cars “toll free” passage.

1.4 – Gilmar Mendes

On Monday, 28th August, STF President Cármen Lúcia asked Judge Gilmar Mendes if he wished to respond to the request by the PRG that he be determined “suspect” regarding his action of issuing habeas corpus for several leaders of the bus transportation cartel in Rio – including Jacob Barata Filho who allegedly has ”close personal relations” with Gilmar and his wife Guiomar.

1.5 – Postalis versus BNY Mellon Bank
Postal, the pension fund of Brazil’s post office employees, allege that it lost some US$ 1.5 billion between 2011 and 2016 (during the presidency of Dilma Rousseff) and that the negligent administration of its funds by BNY Mellon Bank is to blame. Postal hired the law office of Bart S. Fisher in its law suit against BNY Mellon. See Item 1.2.3

1.6 – Joaquim Barbosa as write-in candidate in 2018?

Several times, former STF President, Judge Joaquim Barbosa (now retired from the Supreme Court) has indicated that he might become a candidate for President in 2018, but is not attracted to any current political party. To this end the STF has a case under deliberation that would all “write-in” candidates for president in 2018 – candidates with no party affiliation. The reporter on this case is Judge Luís Roberto Barroso who reportedly is “sympathetic” regarding Barbosa’s candidacy.

Joaquim Barbosa & Luís Roberto Barroso

1.7 – Party migrations

This is the “season” for party migration (switching). Because about one-half of the PSB deputies are discontent with their party’s leadership, some 18 PSB deputies are considering switching – either to the DEM or to the PMDB. On 31st August, father and son switched PSB PMDB – Minister of Mines & Energy Fernando Bezerra Coelho Filho and his father Senator Fernando Bezerra Coelho – both from Pernambuco. The DEM was very upset because their leaders hoped that all PSB dissidents would switch to the DEM.

1.8 – Electricity supply

Because many hydro electric reservoirs are severely depleted (nearly empty), the OAS had activated all the gas turbine generating plants in order to maintain supply. This was not enough, and so this week all generation plants using fuel oil were activated. On 30th August, Petrobras affirmed that because of this sudden increase of fuel oil use, that the supply of fuel or ships was in short supply. Ships use a mixture of fuel oil and diesel.

2 – FOREIGN RELATIONS & TRADE

2.1 – Pres. Temer China
On Tuesday, 29th August, Pres. Temer embarked for a seven-day trip to China – to attend the XI Summit of the BRICS in Xiamen on 31st August, meetings with Chinese authorities including President Xi Jinping, and encounters with Chinese investors interested in the new privatization agenda in Brazil. He is scheduled to return to Brazil on 5th September.

On Sunday, 27th August, Temer met with Chamber President Rodrigo Maia (DEM-RJ) to discuss the agenda for approval of important measures by the Lower House. Maia will become acting president in Temer’s absence.

Because the First Vice-President of the Chamber, Dep. Fábio Ramalho (PMDB-MG) will travel with Temer to China, the Second Vice-President Dep. André Fufuca (PP-MA) will preside over the Chamber during this period. Dep. Fufuca, age 28, is serving his first term as federal deputy (elected in 2014). Apparently, no important measures will be put to a vote in the Chamber because Thursday, 7th September is National Independence Day and probably no quorums will be achieved on 5-6 September.

At the insistence of First Lady Marcela Temer, the President used the *AeroLula* Airbus presidential plane that requires two refueling stops – because it has special private quarters for the first couple. The “new”, larger Boeing 767-300ER presidential jet does not have these accommodations and will be used to transport the presidential entourage – with only one refueling stop en route to China.

Temer’s first refueling stop over was Lisbon (arrived at 10:40 p.m. local time), where he and Marcela stayed at the most expensive luxury hotel in Lisbon (Ritz Four Seasons) -- out of the range of the government’s self imposed “austerity” according to the Brazilian press. **Detail:** In January 2011, then President Dilma Rousseff stayed at the same hotel during a “pit stop” of her return flight from the WEF meeting in Davos.

On Wednesday morning (before resuming his flight to Peking), Temer met with Portuguese President Marcelo Rebelo de Sousa at the Belém Palace (a good excuse for this “pit stop” in Lisbon). According to Temer, Portugal supports Brazil’s membership in the OECD. Also, Portugal confirmed that it would purchase six Embraer KC-390 cargo planes.

OECD ➔ Apparently, Brazil’s “complicated” tax system is one of the main barriers for Brazil to be accepted as a full member of this organization.

**Itaipu—Three Gorges.** On 1st September, in Peking, the Itaipu High Power dam signed an agreement with the China Three Gorges Corp. for cooperation and interchange of technologies, training of engineers, seminars, etc.

During his meeting with Chinese President Xi Jinping, Pres. Temer was advised that China will increase its meat imports from Brazil.

### 2.2 – August trade surplus

On 1st September, MDIC released the trade data for the month of August ➔ US$ 5.599 billion. Exports totaled US$ 19.475 billion (+14.7% YoY while imports were US$ 13.876 billion (+8.0% YoY).
The trade surplus in 2017 is now US$ 48.109 billion (a record since this data series began in 1989) and surpassed the total trade surplus in 2016 (US$ 47.7 billion). MIDIC projects the 2017 total trade surplus at US$ 60 billion.

3 – REFORMS

3.1 – Chamber approved TLP

On Wednesday, 30th August, the Chamber approved the new TLP [Long Term] interest rate that will replace the TJLP [Long Term Interest Rate]. The TJLP was a “very” subsidized interest rate ➔ 7% per year. The new TLP was designed to approximate long term rates used by commercial banks ➔ 9.5%, close to the current Selic basic interest rate (9.25%). This measure now goes to the Senate. Because this is a MP, the limit for Senate approval is 7th September.

The TLP will reduce federal expenditure via subsidies for BNDES loans. The government estimates that over ten years some R$ 240 billion will be saved.

4 – PRIVATIZATION & REGULATION

4.1 - Eletrobras

The proposed privatization of Eletrobras has generated conflicts – especially in the PMDB and PT – the two parties with the largest number of political appointees in this large state enterprise. The PSDB also has a considerable number of political appointees.

However, a study (compiled by 3G Radar) released on 25th August shows that Eletrobras has lost some R$ 4 billion per year due to this over load of incompetent and inadequate political appointees, and an over load of too many employees. Over the past 15 years, Eletrobras lost some R$ 85 billion.

3G compared recent privatizations in this sector in this sector in 1999 ➔ the privatized firms paid more federal taxes and dividends to investors and invested R$ 65 billion, while Eletrobras invested R$ 84 billion.


5 - ECONOMICS

5.1 – GDP data for 2nd Q/2017

On 1st September, IBGE released the GDP data for 2nd Q/2017 ➔ +0.2% and +0.3% for the first semester 2017. For the past 12 months, GDP declined -1.4%. In the second quarter, the services
sector increased by +0.6%, buy declined by -0.3% YoY. The bumper harvests in the first quarter accelerated the agriculture sector by +13.4%, but this sector was stagnant in the second quarter. After nine quarters in decline, in 2nd Q/2017, family consumption increased by +1.4%. The industrial sector continued in decline in the second quarter ➔ -0.5% QonQ and -2.1% YoY.

Finance Minister Henrique Meirelles affirmed that the GDP data for 2nd Q/2017 show that Brazil’s economy is finally surpassing its worst recession in history. However, IBGE said that it is too early to conclude that Brazil’s economy “has recovered”. According to IBGE’s coordinator of national accounts, Rebeca de La Roque Pali, “This is a positive variation, but we can’t call this ‘growth’, until Brazil attains +0.5% sustained growth [per quarter]”.


5.2 – July Public Accounts

Primary Deficit ➔ In July, the central government deficit was -R$ 20.152 billion, the worst result for July in 21 years. The deficit in 2017 is now -R$ 76.277 billion and the 12-month accumulation reached -R$ 183.7 billion (2.84% of GDP). In order to comply with the new deficit target of -R$ 159 billion, the government expects special revenues for concessions and privatizations be the end of 2017.

The Primary Deficit for Brazil (Union, States, Municipalities and State Enterprises) was less in July ➔ -R$ 16.1 billion and the 2017 accumulation was -R$ 51.3 billion. The 12-month accumulation was -R$ 170.5 billion (2.66% of GDP).

Social Security Deficit ➔ -R$ 13.517 billion, and -R$ 96.38 billion in 2017 that contributed to elevating the primary deficit.

Public Debt – R$3.341 trillion (-0.48% MoM)
➔ R$17.68 billion interest paid on this debt in July.

FX Flows ➔ As of 25th August, the Central Bank reported a net inflow of +US$ 4.690 billion.

5.3 – August Inflation

On 30th August, the FGV released its IGP-M ➔ +0.10% after 4 months of deflation. This index is used to readjust rents and in 2017 accumulated -2.56% and -1.71% in 12 months.

<table>
<thead>
<tr>
<th>IGP-M Components</th>
<th>July</th>
<th>August</th>
</tr>
</thead>
<tbody>
<tr>
<td>IPA-Producer Prices</td>
<td>-1.16%</td>
<td>-0.05%</td>
</tr>
<tr>
<td>IPC-Consumer Prices</td>
<td>+0.04%</td>
<td>+0.33%</td>
</tr>
<tr>
<td>INCC-Construction Costs</td>
<td>+0.22%</td>
<td>+0.40%</td>
</tr>
<tr>
<td>IGP-M</td>
<td>-0.72%</td>
<td>+0.10%</td>
</tr>
</tbody>
</table>

5.4 – July tax revenues
On 25th August, the SRF announced that federal tax revenues totaled R$ 109.94 billion – the worst July result in seven years. The accumulated revenues collected in the first 7 months of 2017 total R$ 758.533 billion (-0.61% YoY) – also the worst result since 2010.

5.4.1 – Revenues “frustrated”

The government had positive expectations for a R$ 38.5 billion increases in sources of revenues in 2017, but unfortunately these have been frustrated and threaten the “new” fiscal target. In January-July 2017, “obligatory expenditures” increased by +6.2% (especially the social security deficit and federal employees’ salaries. Other “threats” come from the Refis battle and the attempt to hold new concession auctions the Cemig hydro installations.

5.5 – IIE-Br

On 30th August, the FGV released its Index of Economic Uncertainty for August ➔ 130.1 points, down by -5.9 points from July. FGV began listing the IIE-Br as one of its indicators at the end of 2016.

The IIE-Br has three components: 1) IIE-Br Media that maps stories regarding “economic uncertainty” in the principal newspapers and magazines; 2) IIE-Br Expectations that is constructed via the “dispersion” of projections of the FX rate and the IPCA; and 3) IIE-Br Market based on the volatility of financial markets.

5.6 – Unemployment declined

On 31st August, IBGE released its PNAD unemployment data for May-June-July ➔ 12.8% (13.326 million), down from 13.3% in the quarter ending in April 2017. In the quarter ending in July 2016 the unemployment rate was 11.6%. This decline was large part due to an increase of informal activities where many unemployed encountered opportunities in the informal sector.

In this quarter, IBGE found that 425,000 jobs had been created in the industrial sector and 226,000 jobs in the retail sales area.

5.7 – Auto sales increased in August

According to Fenabrave, in August 216,500 units were sold – the best monthly result since December 2015 (227,800 units).